

Preliminary Draft
**Recommendation to Raise the Capitalization Threshold to \$50,000 for
Property, Plant and Equipment**

Summary

We recommend that the Department of Energy (DOE) consider raising the capitalization threshold to \$50,000 for Property, Plant and Equipment (PP&E). The resulting change in value of fixed assets reported in the financial statements should be immaterial. For Lawrence Livermore National Laboratory (LLNL), for example, capitalizing at this threshold would still include 98% of the current net book value of capital assets and 96% of the current acquisition cost. However, LLNL could reduce the number of reportable capital items and related capitalization oversight activities by 49%.

An analysis should be performed at a complex-wide level for DOE to ascertain the materiality of a threshold change. As a result of raising the threshold, workforce savings would occur for accounting, budget, and program management functions. The existing levels of control should be maintained for the physical accountability of property.

Background

In November 1995, the Federal Accounting Standards Advisory Board issued Statement of Federal Financial Accounting Standards No. 6, "Accounting for Property, Plant, and Equipment." Paragraph 13 states: "The Board believes that capitalization threshold should be established by Federal entities rather than centrally by the Board. Because Federal entities are diverse in size and in uses of PP&E, entities must consider their own financial and operational conditions in establishing an appropriate capitalization threshold or thresholds."

As a result of this standard, DOE raised the capitalization threshold from \$5,000 to \$25,000 at the beginning of fiscal year 1997. In a letter dated August 1, 1996, Elizabeth E. Smedley, the controller, stated: "We believe that this new threshold provides a more appropriate balance between a fair presentation of DOE assets and the related administrative costs that are incurred to achieve proper financial accountability and reporting."

In October 2002, the United States General Accounting Office (GAO) completed a "Survey of Capitalization Threshold and Other Policies for Property, Plant, and Equipment." GAO's report indicates the following:

- Property reporting was one of the main reasons for their disclaiming an opinion on the fiscal year 2001 consolidated statements for the federal government.
- Large increases in capitalization thresholds have occurred for federal agencies since 1997, resulting in significantly higher thresholds than for the private sector which typically use a \$5,000 threshold.

- Operating differences and different financial incentives between the federal government and the private sector could account for the different threshold levels.
- Sharp increases in capitalization thresholds could have a significant effect on the government’s consolidated financial statements.
- The survey was designed to be the first step, a baseline for agencies to analyze the impact of their capitalization thresholds on financial reporting, and not intended to conclude the reasonableness of the threshold levels.
- GAO plans to review the adequacy of capitalization threshold levels in the future.
- The establishment of a capitalization threshold policy must be supported by a detailed analysis, anchored by the fundamental principles of matching and materiality.
- The concept of materiality overlays the matching principle to provide relief from capitalizing and tracking assets that are immaterial to an entity’s financial statements.

Of the 12 private sector companies surveyed, the highest capitalization threshold was \$5,000, whereas federal agency thresholds went as high as \$250,000. The following table shows the capitalization thresholds of the 14 agencies surveyed. Although the Department of Defense was not included in the survey due to limitations pertaining to the reliability of the data, the survey mentions their capitalization threshold of \$100,000.

Federal Agency	Capitalization Threshold
Department of Commerce – National Oceanic and Atmospheric Administrative	\$200,000
Department of Interior	\$15,000
Department of Justice – Bureau of Prisons	\$100,000
Department of Transportation – Federal Aviation Administration	\$25,000
Department of Education	\$50,000
Department of Energy	\$25,000
General Services Administration	\$10,000
National Aeronautics and Space Administration	\$100,000
Social Security Administration	\$100,000
Department of State	\$250,000
Tennessee Valley Authority	\$25,000
Department of Agriculture	\$5,000
United States Postal Service	\$3,000
Department of Veterans Affairs	\$25,000

LLNL Statistics

The following analysis was performed of the Laboratory's fixed assets at different capitalization thresholds.

Capitalization Threshold	Acquisition Cost	% of Current Acq. Cost	Net Book Value	% of Current Net Value	# of Property Items	% of Current #
\$25,000 (current)	\$2,427M	100%	\$1,352M	100%	5,930	100%
\$50,000	\$2,330M	96%	\$1,322M	98%	3,031	51%
\$100,000	\$2,232M	92%	\$1,294M	96%	1,630	27%

Raising the capitalization threshold to \$50,000 would result in a significant effort savings for Accounting functions, such as capitalizations, reconciliations, and funding determinations. In addition, Budget and Programmatic staff would be involved in fewer funding realignments between operating and capital funding. The Laboratory Programs would have fewer accounts and budgets to maintain. Smaller Institutional General Purpose Equipment purchases and Institutional General Plant Projects would no longer be needed, changing the focus to projects of more significance.

Recommendation

In light of the National Nuclear Security Administration's Workload Reduction Initiative and reorganization, we suggest now is an appropriate time to reevaluate the capitalization threshold and determine whether raising the threshold will provide a better balance between financial statement representation of the DOE's assets and the associated administrative costs. We recommend a \$50,000 threshold based on the immateriality of the impact of this change on LLNL's fixed asset value. A DOE-wide analysis should be performed to ensure this level does not result in a material impact to the fixed assets reported in the consolidated financial statements. Consideration should also be given to raising the capitalization threshold to \$100,000, although, this may result in too significant a decrease in asset value and the quantity of capital assets reported by DOE. The existing levels of control should be maintained for the physical accountability of property.